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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1936.

No. [redacted] 21

HERMAN C. GROMAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION OF HERMAN C. GROMAN FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

AND

BRIEF IN SUPPORT THEREOF.

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IN THE

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OCTOBER TERM, A. D. 1936.

No. _____

HERMAN C. GROMAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI.

Your petitioner, Herman C. Groman, respectfully files and submits this as his petition for a writ of certiorari to review the decision and judgment of the United States Circuit Court of Appeals for the Seventh Circuit entered in the above entitled cause on November 30, 1936, reversing the judgment of the United States Board of Tax Appeals. Petition for rehearing, filed December 19, 1936, within the period allowed by the rules of the Circuit Court of Appeals, was entertained, and was denied on January 7, 1937. (R. 48.)

QUESTIONS PRESENTED.

1. Whether or not Section 112 (i) (2) of the Revenue Act of 1928 is an exclusive definition of the term "party to a reorganization."

2. Whether or not a corporation which organizes a sub-

sidiary corporation pursuant to an agreement with stockholders of a third corporation and causes all of the preferred stock of such subsidiary, together with 5,275 shares of prior preference stock of the parent corporation and an amount in cash, to be delivered to the stockholders of the third corporation in exchange for the transfer of their stock to the subsidiary, is a party to a reorganization within the provisions of Section 112 (b) (3), Section 112 (c) (1) and Section 112 (i) of the Revenue Act of 1928.*

Statement.

The Glidden Company (hereinafter called Glidden) contracted with all the stockholders of Metals Refining Company (hereinafter called Indiana) to organize a new subsidiary of Glidden (hereinafter called Ohio). The Indiana stockholders (of whom petitioner is one) were to transfer to Ohio all their stock in Indiana, and Glidden was to give them in exchange, directly and through Ohio, 5,275 shares of prior preference stock of Glidden, 5,000 shares of preferred stock of Ohio, and an amount of cash, computed under the contract terms, which Glidden was to pay Ohio for all the Ohio common stock. All this was done. (R. 13.) The cash received by the Indiana stockholders is concededly taxable to the extent of the gain included therein; the preferred stock of Ohio is concededly received without recognition of gain or loss; and whether the Glidden stock is so received depends upon whether Glidden was "a party to a reorganization" within the meaning of the Revenue Act of 1928; this question, in turn, depends upon the proper interpretation of the provisions of Sec. 112 (b) (3), Sec. 112 (c) (1), and Sec. 112 (i) of that act.

* The relevant sections are reprinted as an appendix to our brief.

Reasons for Granting Writ.

There is a direct conflict in the decisions of the Circuit Courts of Appeals in different circuits on the precise question here involved. In *Commissioner of Internal Revenue* v. *Fifth Avenue Bank, Executor,* 84 F. (2d) 787, the Third Circuit accepted the interpretation, stated by the Board of Tax Appeals and acquiesced in by the Commissioner, that Section 112 (i) (2) was an enumeration and inclusion of certain doubtful cases and not an exclusive definition of the term "a party to a reorganization." This interpretation was followed by the Board of Tax Appeals in *Independent Oil Company,* 35 B. T. A. 32, and in *Claude Neon Lights, Inc.,* 35 B. T. A., No. 63. In *Sage* v. *Commissioner,* 83 F. (2d) 221, the Second Circuit had placed upon the section the same interpretation. In the instant case the Seventh Circuit has interpreted the section in question as containing an exclusive Congressional definition of the words "a party to a reorganization." Since the decision in this case the Third Circuit, in *Commissioner of Internal Revenue* v. *Bashford,* 87 F. (2d) 827, has reasserted its viewpoint and has specifically disapproved and declined to follow the opinion of the Seventh Circuit in the case at bar, stating in the opinion:

> "It seems to us that this fact [that Section 112 (i) (2) is not an all-inclusive definition] was overlooked by the Circuit Court of Appeals for the Seventh Circuit in *Commissioner of Internal Revenue* v. *Groman,* 86 F. (2d) 670, decided November 30, 1936. Consequently we cannot follow the reasoning of that case, but are constrained to hold that one who is a party to a reorganization transaction as that language is commonly understood is a party within the meaning of the statute."

There is involved in this case an important question of federal law which has not been, but which should be, set-

tled by this court. In the group of five cases decided by this court December 16, 1935 (*Nelson Co.* v. *Helvering,* 296 U. S., 374; *Helvering* v. *Minnesota Tea Co.,* 296 U. S. 378; *Helvering* v. *Watts,* 296 U. S. 387; *G. & K. Manufacturing Co.* v. *Helvering,* 296 U. S. 389; and *Bus & Transport Securities Corp.* v. *Helvering,* 296 U. S. 391), numerous questions involving the reorganization sections of various revenue acts were discussed and determined; but the precise question here raised (the interpretation of Section 112 (i) (2) of the 1928 Act) was not disposed of. We believe, however, that the decisions in *Nelson Co.* v. *Helvering* and *Helvering* v. *Minnesota Tea Co.* and the opinion in *Pinellas Ice Co.* v. *Commissioner,* 287 U. S. 462 (pp. 469-70), are applicable decisions of this court, and that the decision of the Circuit Court of Appeals for the Seventh Circuit is probably in conflict therewith, since the interpretation of Section 112 (i) (2) in the instant case is inconsistent with the construction of Section 112 (i) (1) by this court in the cases cited. A specific and authoritative determination of the proper construction of this section is a matter of great importance in the construction of the taxing statutes, particularly since the same problem is presented under all the revenue acts since 1928.

The decision in this case is directly in conflict with the regulations of the Treasury Department in force from 1924 to 1933 (Reg. 65, Art. 1577; Reg. 69, Art. 1577; Reg. 74, Art. 577; Reg. 77, Art. 577) (quoted in our brief at p. 16) and the uniform holdings of the Board of Tax Appeals (*Tulsa Oxygen Co.,* 18 B. T. A. 1283; *John S. Woodard,* 30 B. T. A. 1216; *Fifth Avenue Bank of New York, Executor,* 31 B. T. A. 945; *Raymond I. Bashford,* 33 B. T. A. 10; *Independent Oil Co.,* 35 B. T. A. 32). In *Claude Neon Lights, Inc.,* 35 B. T. A., No. 63, the Board refers to this case as contrary to other authorities, and does not follow it.

Specification of Errors.

The Circuit Court of Appeals for the Seventh Circuit erred:

1. In reversing the decision and order of the Board of Tax Appeals.

2. In holding that Section 112 (i) (2) of the Revenue Act of 1928 is an exclusive definition of the words "a party to a reorganization."

3. In holding that the Glidden Company was not a party to a reorganization within the meaning of Section 112 (b) (3), Section 112 (c) (1), and Section 112 (i) of the Revenue Act of 1928.

4. In failing to hold that the prior preference stock of the Glidden Company received by petitioner was "stock or securities * * * in another corporation a party to the reorganization" within the meaning of the language of Section 112 (b) (3) and Section 112 (c) (1) of the Revenue Act of 1928.

5. In holding and finding that the prior preference stock of the Glidden Company received by petitioner was "other property" within the meaning of Section 112 (c) (1) and that petitioner's gain was recognizable to the extent of the value of these shares.

Wherefore your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Seventh Circuit commanding that court to certify and to send to this court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket No. 5779, Commis-

sioner of Internal Revenue *vs.* Groman, and that the said judgment of the said Circuit Court of Appeals for the Seventh Circuit may be reversed by this Honorable Court and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

HERMAN C. GROMAN,
By EGBERT ROBERTSON,
JAMES C. SPENCE,
His Attorneys.

DAVID L. KREBS,
HENRY L. MCINTYRE,
Of Counsel.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

THE OPINIONS OF THE COURTS BELOW.

The opinion of the Board of Tax Appeals in this case was filed on June 17, 1935, and is not reported, but may be found at pages 10-18 of the record herein.

The opinion of the Circuit Court of Appeals for the Seventh Circuit appears in the record at pages 43-47, and is reported in 86 F. (2d) 670.

II.

JURISDICTION.

1. The judgment of the Circuit Court of Appeals was entered on November 30, 1936. (R. 43.) Petition for rehearing was filed December 19, 1936 (R. 48), within the time provided by the Rules of the Circuit Court of Appeals, was entertained, and was denied January 7, 1937. (R. 48).

2. The jurisdiction of this court is based upon Judicial Code, Section 240(a), as amended by the Act of February 13, 1925, c. 229, § 1, 43 Stats. 938; 28 U. S. C. A. § 347.

3. Since the case is not one of those reviewable by appeal, it seems unnecessary to cite decisions in support of the jurisdiction of the court by certiorari, as to which the statute confers an unlimited discretion. The propriety of the exercise of such jurisdiction in this case is supported by the opinion in *Duparquet Co.* v. *Evans,* 297 U. S. 216. It is there said:

> "Because of this conflict [between Circuits] and because of the importance of removing doubt as to the meaning of the statute, a writ of certiorari was granted by this court" (p. 217).

III.

STATEMENT OF THE CASE.

The facts are summarized in the petition, but we think it advisable to set them out here more in detail.

The Glidden Company was an Ohio corporation, engaged in the manufacture of paints and varnishes. Metals Refining Company was an Indiana corporation, engaged in the business of refining lead and in the production of various alloys. (R. 11.) In January, 1929, Glidden entered into a contract with all the stockholders of Indiana, which contract recited that,

> "The shareholders are desirous of merging and consolidating the properties of their company with the Glidden Company and with a corporation to be incorporated and organized under the laws of Ohio, such merger or consolidation to be effected in the manner hereinafter set forth." (R. 11),

and provided that the shareholders of Indiana should transfer their shares to an Ohio corporation to be organized by Glidden with a capitalization of 5,000 preferred shares and "such number of common shares, par or non-par, as Glidden Company may determine, all of which shall be acquired by Glidden Company for a cash consideration sufficient to meet the requirement of Section 7 [which provided for the consideration to be paid the shareholders of Indiana]." (R. 12.) Glidden in turn agreed to organize and incorporate the Ohio Company and to cause the assets of Indiana to be transferred to the new company after the stock in Indiana had been received by Ohio.

The contract further provided that Glidden, as a consideration for such consolidation, would issue and deliver, or cause to be delivered, to the Indiana stockholders, securities and cash as follows:

"The sound value of fixed assets of the Indiana Com-

pany is to be determined by the American Appraisal Company of Milwaukee, Wisconsin. The good-will of the Indiana company for the purpose of this agreement shall be valued at Five Hundred Thousand Dollars ($500,000). The book value of all other assets as of March 1, 1929 * * * as approved by auditors selected by the Glidden Company shall be used.

Against the total value of the assets so determined there shall be issued—

(a) Up to 5,275 shares of 7% prior preference stock of the Glidden Company on the basis of One Hundred Five Dollars ($105) per share.

(b) Up to 5,000 shares of the 6% cumulative preferred stock of the new Ohio Company, hereinbefore referred to, on the basis of One Hundred Dollars ($100) per share.

(c) After deducting from the total value of such assets the amount of prior preference stock and preferred stock issued on the basis above set forth, the remaining value of such assets shall represent the amount of cash payable to the shareholders of the Indiana Company on the consummation of such consolidation." (R. 13.)

This contract was performed and Indiana was thereafter dissolved. (R. 13.) Petitioner owned 500 shares of stock in Indiana and by virtue of the above transactions, he received in exchange therefor 565 shares of preferred stock of Ohio, 596 shares of prior preference stock of Glidden, and $17,293.14. (R. 7-8.)

As the Circuit Court of Appeals said:

> "It is admitted that the cash received by stockholders was taxable and also that respondent's [petitioner's] proportion of the 5,000 shares of the preferred stock of the new Ohio Company by him received was not taxable. The issue was limited to respondent's [petitioner's] proportion of 5,276 shares of preferred stock of Glidden Company." (R. 44.)

The Commissioner determined that the Glidden Company was not a party to the reorganization. (R. 5-8.) The Board

of Tax Appeals determined otherwise and held that the Glidden stock was received by petitioner without recognition of gain. (R. 18.) This decision of the Board of Tax Appeals was reversed by the Circuit Court of Appeals. (R. 47.)

Proceedings in the cases of six other stockholders of Indiana as to whom petitions for review of the decision of the Board of Tax Appeals were filed in the Circuit Court of Appeals for the Seventh Circuit were suspended by order of the Circuit Court of Appeals to abide the final decision in this case. (R. 37.)

IV.

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals for the Seventh Circuit erred:

1. In reversing the decision and order of the Board of Tax Appeals.

2. In holding that Section 112 (i) (2) of the Revenue Act of 1928 is an exclusive definition of the words "a party to a reorganization."

3. In holding that the Glidden Company was not a party to a reorganization within the meaning of Section 112 (b) (3), Section 112 (c) (1), and Section 112 (i) of the Revenue Act of 1928.

4. In failing to hold that the prior preference stock of the Glidden Company received by petitioner was "stock or securities * * * in another corporation a party to the reorganization" within the meaning of the language of Section 112 (b) (3) and Section 112 (c) (1) of the Revenue Act of 1928.

5. In holding and finding that the prior preference stock of the Glidden Company received by petitioner was "other property" within the meaning of Section 112 (c) (1) and that petitioner's gain was recognizable to the extent of the value of these shares.

V.

STATUS OF LOWER COURT DECISIONS.

The question of who is a party to a reorganization has been considered in five Circuit Courts of Appeals decisions:

C. H. Mead Coal Co. v. *Commissioner,* 72 F. (2d) 22, (C. C. A. 4, 1934);

Sage v. *Commissioner,* 83 F. (2d) 221, (C. C. A. 2, 1936);

Commissioner v. *Fifth Avenue Bank, Executor,* 84 F. (2d) 787, (C. C. A. 3, 1936);

Commissioner v. *Groman,* 86 F. (2d) 670, (C. C. A. 7, 1936—this case);

Commissioner v. *Bashford,* 87 F. (2d) 827, (C. C. A. 3, 1937).

The Seventh Circuit in the instant case held that Section 112 (i) (2) is an exclusive definition of the words "a party to a reorganization" and that there can be no parties to a reorganization other than those there enumerated. The Second, Third and Fourth Circuits have held that this is not an exclusive definition. The Second Circuit has suggested that "a party to a reorganization" is one of the necessary parties to a transaction detailed in Section 203 (h) (1) of the 1926 Act, (Section 112 (i) (1) of the 1928 Act) (*Sage* v. *Commissioner,* 83 F. (2d) at 223, 224). The Third Circuit has emphasized as tests (1) the degree of participation taken in the reorganization (*Commissioner* v.

Bashford, 87 F. (2d) at 830) and (2) the presence of continuity of interest in the assets transferred (*Commissioner* v. *Fifth Avenue Bank, Executor,* 84 F. (2d) at 789). The Fourth Circuit seems to have relied upon both these tests (*C. H. Mead Coal Co.* v. *Commissioner,* 72 F. (2d) at 29).

VI.

SUMMARY OF ARGUMENT.

Point A. Section 112 (i) (2) of the 1928 Act is not an exclusive definition of the term "a party to a reorganization." The Revenue Act itself provides otherwise. The language is not that of a definition. This court has otherwise interpreted like language in Section 112 (i) (1). Treasury regulations under prior acts, the interpretation of which Congress has adopted by the re-enactment of this section after the promulgation of such regulations, specifically repudiate this interpretation. Circuit Courts of Appeals in other circuits, the uniform decisions of the Board of Tax Appeals, and the views of text-writers are all to the contrary.

Point B. In determining whether a corporation is a party to a reorganization the applicable criteria are the participation of such corporation in the reorganization and a continuity of interest of the transferors, through ownership of stock in the corporation whose participation is involved, in the assets transferred.

Point C. Glidden was a party to the reorganization between Indiana and Ohio because it participated therein, and, indeed, dominated and directed the proceedings, and because the Indiana stockholders received and retained an interest in the assets transferred by Indiana through the acquisition by them of stock in Glidden representing a defi-

nite and material interest in Glidden, and through Glidden in Ohio, and a substantial part of the value of the transferred assets.

Point D. The transaction here involved may logically be regarded as a direct reorganization between Glidden and Indiana, and Ohio may be treated as an instrumentality and *alter ego* of Indiana, whose corporate entity may under settled rules of decision be disregarded to give effect to the substance rather than the form of the transaction.

VII.

ARGUMENT.

Point A.

SECTION 112 (i) (2) OF THE 1928 ACT IS NOT AN EXCLUSIVE DEFINITION OF THE TERM "A PARTY TO A REORGANIZATION."

Section 112 (i) of the Revenue Act of 1928 provides:

> "(i) DEFINITION OF REORGANIZATION. As used in this section and sections 113 and 115—
>
> "(1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.
>
> "(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation."

The Circuit Court of Appeals herein has concluded that in Section 112 (i) "Congress • • • saw fit to define with particularity the terms 'reorganization' and 'parties to a reorganization'." (R. 47.) We do not quarrel with the first conclusion but we cannot agree that Congress has attempted to *define* even vaguely the term "a party to a reorganization."

Section 701 (b) of the Revenue Act of 1928 provides:

> "The terms 'includes' and 'including' when used in a definition contained in this Act shall not be deemed to exclude other things otherwise within the meaning of the term defined."

A similar provision is also found in Section 2 (b) of the Revenue Act of 1926. So, even if Section 112 (i) (2) can be regarded as a "definition" at all, it cannot be considered as a complete and exclusive one in view of this specific language of the statute. But it is by no means certain that Congress intended to define anything when it enacted Subsection 112 (i) (2). Section 112 (i) is entitled "DEFINITION OF REORGANIZATION." There is nothing in this designation to indicate that it was also the intention of Congress to define "a party to a reorganization."

Section 112 (i) (1) begins "The term 'reorganization' *means* * * *." The distinction is clear cut between the use of the word "means" here and the use of the word "includes" in Section 112 (i) (2) which begins "The term 'a party to a reorganization' *includes* * * *." Section 112 (j) is entitled "DEFINITION OF CONTROL." This section again begins "As used in this section, the term 'control' *means* * * *." It is very apparent, therefore, that Congress has carefully distinguished between the word "means" and the word "includes" in this statute, and that the word "includes" is not used in a restrictive or limiting sense.

This court has marked the distinction in the opinions in *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, and *Pinellas Ice Co.* v. *Commissioner*, 287 U. S. 462. Those cases concerned the interpretation of the words "merger or consolidation (*including* the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes

of stock of another corporation, or substantially all the properties of another corporation)'' contained in Section 112 (i) (1) of the 1928 Act and the same words in Section 203 (h) (1) (a) of the 1926 Act. It was urged in those cases that the words within the parenthesis following the word ''including'' were restricted and limited by the words ''merger'' or ''consolidation'' immediately preceding the parenthesis, but this court rejected that contention and said (296 U. S. at 385, 287 U. S. at 469-470):

> ''The words within the parenthesis may not be disregarded. They expand the meaning of 'merger' or 'consolidation' so as to include some things which partake of the nature of a merger or consolidation but are beyond the ordinary and commonly accepted meaning of those words—so as to embrace circumstances difficult to delimit but which in strictness cannot be designated as either merger or consolidation.''

The provisions of Section 112 (i) (2) of the Revenue Act of 1928 first appeared in their present form in Section 203 (h) (2) of the Revenue Act of 1924. Regulations 65 relating to income taxes under the Revenue Act of 1924 contained Article 1577, reading as follows:

> ''The term 'a party to a reorganization,' as used in sections 201, 203, and 204 includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation. *This definition is not an all-inclusive one, but simply enumerates certain cases with respect to which doubt might arise.*'' (Italics added.)

The exact language of Section 203 (h) (2) of the Revenue Act of 1924 (which is identical with the language of Section 112 (i) (2) of the 1928 Act) was re-enacted in the Revenue Act of 1926, and Regulations 69 under the 1926 Act contain the same Article 1577 above quoted. Exactly the same lan-

guage is found in Article 577 of Regulations 74 under the 1928 Act.

Congress, by enacting the 1926 and 1928 Acts in the same language as that of the 1924 Act, has adopted the interpretation given this language by the original treasury regulations. The regulations construing the 1924 and 1926 Acts must have been well in mind when the 1928 Act was enacted. This court has recognized the effect of such Congressional re-enactment of a statute as an approval of the construction contained in the income tax regulations, in the cases of *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, at 384; *Helvering* v. *Watts*, 296 U. S. 387, at 389, *Morrissey* v. *Commissioner*, 296 U. S. 344 at 355, and *Helvering* v. *Bliss*, 293 U. S. 144 at 151.

The opinion of the Circuit Court of Appeals is clearly contrary to these regulations and the will of Congress as indicated by the re-enactment of this same provision after the regulation had been in effect for four years.

The opinion of the Circuit Court of Appeals for the Third Circuit in *Commissioner* v. *Fifth Avenue Bank, Executor*, 84 F. (2d) 787, decided prior to the decision of the Circuit Court of Appeals of the Seventh Circuit herein, contains the following at page 789:

> "The Board construes (i) (2) as not all inclusive, and quotes Regulations 74, Art. 577, which says that it 'simply enumerates certain cases with respect to which doubt might arise'."

The same court, in *Commissioner* v. *Bashford*, 87 F. (2d) 827, decided subsequent to the decision of this case by the Circuit Court of Appeals for the Seventh Circuit, again said:

> "The definition contained in the statute is, as this court pointed out in *Commissioner of Internal Revenue* v. *Fifth Avenue Bank of New York*, 84 F. (2d) 787, 789, not an all-inclusive one, but, as petitioner stated in

> his interpretive regulations (Article 577, Regs. 74), it 'simply enumerates certain cases with respect to which doubt might arise.' It seems to us that this fact was overlooked by the Circuit Court of Appeals for the Seventh Circuit in *Commissioner of Internal Revenue* v. *Groman,* 86 F. (2d) 670, decided November 30, 1936. Consequently we cannot follow the reasoning of that case, but are constrained to hold that one who is a party to a reorganization transaction as that language is commonly understood is a party within the meaning of the statute."

The Circuit Court of Appeals for the Second Circuit has also reached this conclusion. In *Sage* v. *Commissioner,* 83 F. (2d) 221, after setting forth Section 203 (h) (2) of the Revenue Act of 1926, that court says:

> "Although the Kimberly Company does not fall within this Section, Article 1577 provides: 'This definition is not an all inclusive one, but simply enumerates certain cases with respect to which doubt might arise.'
>
> "We can therefore look to the definition of a reorganization to determine the status of the Kimberly Company."

The Board of Tax Appeals has also taken this view in numerous cases. The opinion in the instant case, when it was before the Board (R. 11-18), as well as the opinions in the *Fifth Avenue Bank* (31 B. T. A. at 951), *Bashford* (33 B. T. A. at 18) and *Claude Neon Lights, Inc.* (35 B. T. A., No. 63 at 10) cases when they were before the Board, interpreted the statute in question as we contend. A similar statement of the Board's view appears in *John S. Woodard,* 30 B. T. A. 1216, at 1223-24.

In addition to the lower federal courts and the Board of Tax Appeals, text writers have reached the conclusion that this statutory language is not exclusive. (Baar and Morris, "Hidden Taxes in Corporate Reorganizations" (1935), page 148; Paul and Mertens, "Law of Federal Income Taxation" (1934), Vol. 2, page 211.)

The authorities cited in the Seventh Circuit opinion do not sustain that court's view. In *Bus and Transport Securities Corp.* v. *Helvering,* 296 U. S. 391, this court held there was no reorganization at all. In *G. & K. Manufacturing Co.* v. *Helvering,* 296 U. S. 389, this court remanded the cause for a determination of factual questions which would decide whether there was a reorganization, but who were parties to the reorganization (if there was one) was not involved. *Ballwood Co.* v. *Commissioner,* 84 F. (2d) 733, does not discuss the language of Sec. 112 (i) (2), but the decision follows the decision in *Helvering* v. *Minnesota Tea Co.,* 296 U. S. 378, and is squarely in accord with our contention here.

In conclusion, we wish to point out that this court has in effect held that there can be parties to a reorganization other than those enumerated in Section 112 (i) (2). For in the *Minnesota Tea* case (296 U. S. 378), Grand Union acquired all of the property of Minnesota Tea in return for 7½ per cent of its (Grand Union's) stock. Obviously, Grand Union is not "a corporation resulting from a reorganization" and there has been no "acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation." Yet it was held in the *Minnesota Tea* case that the shares of Grand Union were received without recognition of gain. Although the point was not discussed in the opinion, this holding necessarily means that Grand Union was "a party to a reorganization," since otherwise its stock would not have fallen within Section 112 (b) (4).

The effect of the decision in *Nelson Co.* v. *Helvering,* 296 U. S. 374 is the same, since that case involved solely the acquisition of property in return for stock.

We submit that these decisions are determinative of this point on principle, and are applicable here, and that the decision of the Circuit Court of Appeals is in conflict therewith, and erroneous.

Point B.

IN DETERMINING WHETHER A CORPORATION IS A PARTY TO A REORGANIZATION, THE CRITERIA ARE: (1) PARTICIPATION; (2) CONTINUITY OF INTEREST (THROUGH STOCK OWNERSHIP) IN THE ASSETS TRANSFERRED.

1. *Participation as a Test.*

If our argument is correct thus far, the next problem is to determine what are the essentials to qualify a corporation as a party to a reorganization within the meaning of that phrase as used in Section 112. Beginning with the literal sense of the words, we find that Funk and Wagnalls define "party" as "one concerned in or privy to a matter". "*Law* * * * one who is related to or united with another or others in * * * a transaction." Webster says "party" is "one concerned in an affair; a participator; as a *party* in interest, * * * a *party* to a plot",

Clearly under the facts in this case, Glidden comes within this dictionary definition, since it played such an active part in the transactions involved.

But did Congress have in mind, when it used this phrase "party to a reorganization" something different from the usual meaning of the words? The Circuit Court of Appeals for the Third Circuit in *Commissioner* v. *Bashford*, 87 F. (2d) 827, says:

> "We * * * are constrained to hold that one who is a party to a reorganization transaction as that language is commonly understood is a party within the meaning of the statute. * * * we fully agree with the Board that a corporation so intimately connected with the reorganization of the other corporations as

was Atlas in this case, is a party to the reorganization within the commonly understood meaning of that phrase, although not reorganized itself." (Page 830.)

The Board in this case had said (33 B. T. A. 17-18):

"In short, Atlas was the main spring of the entire proceeding and without its participation there would have been no reorganization and consolidation into the new company."

The text writers also emphasize the activity of a particular corporation as indicating its relationship to the reorganization. Thus in Baar and Morris, "Hidden Taxes in Corporate Reorganizations", it is said, at page 147:

"Where, however, a corporation is the principal or dominating actor in the particular transaction which constitutes the reorganization, and *perhaps particularly where it nominates an affiliated corporation to play a role which clearly qualifies the subsidiary as a party,* the other corporation may be recognized as a party to the reorganization even though it does not qualify under the statutory definition or any of the established rules." (Italics added.)

And in Paul and Mertens, "Federal Income Taxation" (1936 Supp. to Volume II) the following appears at page 68:

"Where the corporation is so intimately connected with the reorganization of other corporations that the reorganization depends on its efforts or support, then such corporation is a party to the reorganization although it is not reorganized itself."

In applying this test, which we, for brevity sake, will call "the participation test", we may concede that not every minor participant in a reorganization satisfies this requirement. Thus, as Paul and Mertens point out in Volume II of their work on Income Taxation (page 213):

"It was clearly not the Legislature's intent, for instance, to permit non-recognition of gain upon the exchange of stock of corporation A for the stock of corporation C (which was received in addition to stock of

corporation B) where the reorganization takes the form of a merger of corporation A into corporation B and where corporation C is a minor and incidental participant in the reorganization."

The opinion of the Third Circuit in *Commissioner* v. *Bashford*, 87 F. (2d) 827, sets forth a good general summary of the salient facts which indicate the degree of participation which a particular corporation has taken in the reorganization of another corporation, and points out generally where the line is to be drawn between cases of insufficient participation and those in which the third corporation is in reality the motivating force and *sine qua non* of the reorganization. Thus, the findings of fact of the Board are there set forth as follows:

> "That the entire idea and plan of reorganization, was conceived by Atlas; that it was in the line of Atlas' business; and that its promotion and execution were entrusted to its agents, Seligman and Fletcher under general instructions. The plan was developed and formed by Atlas and its agents; cash and its own stock necessary to the accomplishment of the transaction were furnished by Atlas; and it became the owner of the majority of the voting stock and of all of the preferred stock of the new company. In short, Atlas was the main spring of the entire proceeding and without its participation there would have been no reorganization and consolidation into the new company."

Thus in the discussions of the problem found in the decisions and the text-books, considerable emphasis seems to be placed on the extent or degree of participation of the corporation in question.

2. *Continuity of Interest as a Test.*

An important consideration in all reorganization tax cases as crystallized by the opinions of this court is the "continuity of interest" which must be maintained by the transferror in the assets transferred.

Pinellas Ice Co. v. *Commissioner*, 287 U. S. 462.

Helvering v. *Minnesota Tea Co.*, 296 U. S. 378.
Helvering v. *Watts*, 296 U. S. 387.
Nelson Co. v. *Helvering*, 296 U. S. 374.
Bus and Transport Securities Corp. v. *Helvering*, 296 U. S. 391.

Thus in the *Pinellas* case the court (287 U. S. at 470) says:

> "Certainly we think that to be within the exemption *the seller must acquire an interest in the affairs of the purchasing company* more definite than that incident to ownership of its short-term purchase-money notes." (Italics added.)

and in the *Minnesota Tea Co.* case (296 U. S. at 386):

> "The transaction here was no sale, but partook of the nature of a reorganization in that the seller acquired a definite and substantial interest in the purchaser.
>
> "True it is that the relationship of the taxpayer to the assets conveyed was substantially changed, but this is not inhibited by the statute. Also, a large part of the consideration was cash. This, we think, is permissible so long as the taxpayer received an interest in the affairs of the transferee which represented a material part of the value of the transferred assets."

As it was phrased by the Circuit Court of Appeals for the Fourth Circuit in *C. H. Mead Coal Co.* v. *Commissioner*, 72 F. (2d) 22, 29:

> "If there is not merely a sale of the assets, but a *continuity of interest* on the part of the old stockholder *in the new business*, so that the old stockholder does not actually liquidate his holdings, *but continues to be a participant in the enterprise* without actual realization of profit, and if the transaction partakes of the nature of a merger or consolidation in a liberal view, it is not the purpose of the Act to recognize either a gain or a loss in the transaction, and no such gain or loss will affect the income tax of the stockholder until the new stock or securities are disposed of." (Italics added.)

The same test was applied in *Commissioner* v. *Fifth Avenue Bank, Executor,* 84 F. (2d) 787 at 789.

Accordingly, it seems inevitable that where, in a transfer of assets of Corporation B, Corporation A has furnished the initiative and the means, and has directed the procedure, and where the former stockholders of Corporation B, *through acquisition of stock in Corporation A,* receive and retain a substantial interest in the property and business formerly operated by Corporation B, there is a reorganization, and Corporation A is a necessary party to it.

Point C.

GLIDDEN WAS A PARTY TO THE REORGANIZATION BETWEEN INDIANA AND OHIO.

1. *Glidden Participated in the Reorganization.*

It is conceded that the facts in this case, from one point of view, involve a reorganization between Ohio and Indiana (R. 23). Applying then, the participation test to Glidden in order to determine whether it was a party to this reorganization, we find that the facts show that the contract which is the basis of and gave rise to and contained the plan for the entire reorganization was entered into and executed by Glidden (R. 11-13). The reorganization was in the furtherance of Glidden's business; Ohio was organized by Glidden in accordance with the terms of the contract; Glidden determined the capital structure of Ohio and acquired control of Ohio through the purchase of all its voting stock; Glidden had charge of the audits to determine the value of the Indiana assets; Glidden furnished the necessary cash to pay for Indiana stock and issued its own prior preference stock to Indiana shareholders; and finally, Glidden caused the assets of ~~Ohio~~ INDIANA to be transferred to Ohio, and paid the quarterly dividends upon the preferred stock of Ohio. (R. 4, 13-14, 44.)

To use the language of the Board of Tax Appeals in the *Bashford* case, Glidden, even as Atlas, "was the main spring of the entire proceeding and without its participation there would have been no reorganization and consolidation into the new company" (33 B. T. A. 17-18).

2. *The Continuity of Interest in the Indiana Assets Was Preserved to the Indiana Stockholders by Virtue of Their Acquisition of the Glidden Stock.*

At the beginning of the transactions herein involved the shareholders of Indiana had an equity of $1,207,016.66 in the assets of the Indiana corporation, on the basis of the appraisal made pursuant to the contract between the Indiana stockholders and Glidden. When the reorganization was completed these same shareholders of Indiana had instead of their stock in Indiana $500,000.00 of preferred stock in Ohio, $553,980.00 of prior preference stock in Glidden and $153,036.66 in cash. Expressed in a different fashion, the shareholders' equity in the Indiana assets was now represented roughly, 13% by cash, 45% by prior preference stock in Glidden and 42% by preferred stock in Ohio.

As all of the assets of Indiana had been transferred to Ohio, the equity in the Indiana assets was then represented by the $500,000.00 worth of preferred stock received by the former stockholders of Indiana and 100 shares of common stock of Ohio owned by Glidden. This gave the 100 shares of common stock an equity, based on the appraisal, of $707,016.66. Thus there was a continuity of interest in the Indiana shareholders in the original Indiana assets, not only through their ownership of the Ohio stock but also through their ownership of the Glidden stock, since Glidden through its acquisition of the common stock of Ohio was the owner of all of the equity in the original Indiana assets not represented by the preferred stock of

Ohio. Accordingly, everything that the Indiana shareholders received, aside from cash, represented a substantial interest in the original assets of Indiana. And if they had not received any stock in Glidden they would have lost all their interest in $707,016.66 of the assets transferred.

This Court, in *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, after referring to the rule laid down in *Pinellas Ice Co.* v. *Commissioner*, 287 U. S. 462, that the transferror "must acquire an interest in the affairs of the purchasing company more definite than that incident to ownership of its short term purchase money notes" said that "this interest must be definite and material; it must represent a substantial part of the value of the thing transferred. This much is necessary in order that the result accomplished may genuinely partake of the nature of merger or consolidation".

In *Miller* v. *Commissioner*, 84 F. (2d) 415, the Circuit Court of Appeals for the Sixth Circuit, after discussing the *Minnesota Tea Co.* case, suggested the following definition:

> "In the commonly accepted legal sense, a substantial interest is something more than a merely nominal interest, and, in respect to corporations, a definite and material interest is an interest beyond what is usually referred to as represented by 'qualifying shares.'"

It is clear that the $553,980.00 of stock in Glidden acquired by Indiana stockholders represented "a definite and material interest" in Glidden. It was certainly not a merely nominal interest. It is equally clear that this Glidden stock represents "a substantial part of the value of the thing transferred" as the total value of the assets transferred was appraised at $1,207,016.66. Inasmuch as Glidden had acquired all the common stock of Ohio (representing $707,016.66 of Indiana's assets), the interest received by Indiana's shareholders in Glidden is just as definite and ma-

terial an interest in the "affairs of the purchasing company" and represents just as substantial a "part of the value of the thing transferred" as if Glidden had received the $707,016.66 of the assets themselves, rather than the equity in such assets in the form of this common stock. Since the common stock of Ohio carried all the voting power, Glidden was in complete control of Ohio and the stockholders in Glidden had an interest in the "affairs" of Ohio. This court in laying down the rule has not required that the interest retained be a stock interest in the purchasing corporation itself, but rather the interest must be an "interest in the *affairs* of the purchasing corporation." It cannot be doubted that holders of a substantial amount of stock in a parent corporation have a definite and material interest in the affairs of the parent's subsidiary. Hence, to use the language of the *Minnesota Tea Co.* opinion, everything necessary has been done so that "the result accomplished may genuinely partake of the nature of merger or consolidation". This result is accomplished through the acquisition by the petitioner of the Glidden stock. For this reason we feel that the receipt of the stock in Glidden constitutes just such an exchange as Congress intended should be tax-free.

The reorganization sections of the Revenue Acts since 1918 have been intended to relieve against oppressive and premature taxation where there has been a mere change in form as regards the interest of the taxpayer in his property. In *Cortland Specialty Co.* v. *Commissioner,* 60 F. (2d) 937, it is stated as follows:

> "Its purpose was to relieve those interested in corporations from profits taxes in excess where there was only a change in corporate form in which it was conducted without an actual realization of any gain from an exchange of properties. * * * Reorganization presupposes continuance of business under modified corporate forms". See also, *C. H. Mead Coal Co.* v. *Commissioner,* 72 F. (2d) 22, at 27-8.

The stockholders of Indiana at the completion of the transaction under scrutiny were clearly continuing the business under modified corporate forms—instead of acting in the form of Indiana, they were now acting in the form of Glidden and its wholly owned subsidiary, Ohio.

We have set forth and discussed above what appeals to us as the essential criteria in the mind of Congress and as developed by the decisions as to who were to be considered parties to a reorganization. It may be argued by the Commissioner that one of the tests that should be considered in determining whether a corporation is a party to a reorganization is whether such corporation's structure is directly affected in some manner. It is true that in numerous reorganizations unquestionably coming within the statutory definition, the corporate structure is either directly affected or there is a transfer of a substantial portion of the outstanding stock of such corporation. If this test is applied to Glidden it will be found that its corporate structure is affected. An additional 5,275 shares of preferred stock were issued. This increased its outstanding preferred stock by more than 7 per cent. And in the *Minnesota Tea* case 7½ per cent of the Grand Union stock was exchanged.

Point D.

THE TRANSACTION HERE INVOLVED, IN SUBSTANCE, IS A REORGANIZATION BETWEEN GLIDDEN AND INDIANA WITHIN THE MEANING OF SECTION 112 (i) (1) OF THE REVENUE ACT OF 1928.

Thus far we have treated the facts of this case as though they involved a reorganization between Ohio and Indiana, but the case may be equally regarded as a reorganization between Glidden and Indiana.

The preamble of the contract entered into between Glid-

den and the shareholders of Indiana recites that "the shareholders are desirous of merging and consolidating the properties of their company with the Glidden Company and with a corporation to be incorporated and organized under the laws of Ohio, such merger or consolidation to be effected in the manner hereinafter set forth". Thus it appears that at the outset the declared purpose was to effect a merger between Glidden and Indiana. The manner by which this plan was carried through and the use of the Ohio corporation prevent the transaction's being a *statutory* merger or consolidation. But this court pointed out in *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, that the words "including the acquisition by one corporation of * * * substantially all the properties of another corporation" are not limited to acquisitions in the course of purely statutory mergers or consolidations. It is now settled that any such acquisition which is of the nature of a merger or consolidation falls within the definition in the Revenue Act. Clearly, if the Ohio corporation had never been formed, and if the stock of Indiana had been transferred directly to Glidden solely in return for Glidden stock, it would never have been contended that the transaction was not within the meaning of Section 112 (i) (1) (A). The existence of Ohio, then, as a separate corporation, is the only thing that can be thought to prevent the transaction from falling within this definition. But this court in the case of *Southern Pacific Co.* v. *Lowe*, 247 U. S., 330, laid down the rule that the separate corporate existences of a parent and a wholly owned subsidiary will be looked through if they are in fact and for all practical purposes merged into one unit, the subsidiary being but a part of the parent and subject in all things to the direction and control of the parent. The question in the *Southern Pacific* case was whether dividends received by the parent

from the subsidiary in 1914 were subject to the income tax of 1913. The facts showed that the dividends were paid out of a surplus that had accrued to the subsidiary prior to 1913. After pointing out the facts indicating the close relationship and identity of interest between the two corporations, this court said (pages 335-6):

> "* * * we deem it to be equally clear that this surplus accrued to the Southern Pacific Company prior to that date, in every substantial sense pertinent to the present inquiry, and hence underwent nothing more than a change of form when the dividends were declared."

This was true because the Central Pacific and the Southern Pacific were in substance identical because of the complete ownership and control which the latter possessed over the former as a stockholder and in other capacities.

The case of *Gulf Oil Corporation* v. *Lewellyn*, 248 U. S. 71, expanded the rule of the *Southern Pacific* case. In the *Gulf Oil* case the parent company was held not to be taxable upon dividends paid by its subsidiary out of funds acquired prior to the taxable year. The court said:

> "The petitioner did not itself do the business of its subsidiaries and have possession of their property as in *Southern Pacific Co.* v. *Lowe*, 247 U. S. 330, but the principle of that case must be taken to cover this." (pp. 72-73).

It is true that the case of *Burnet* v. *Commonwealth Improvement Co.*, 287 U. S. 415, has pointed out the limits to which this rule can be expanded:

> "*Southern Pacific Co.* v. *Lowe, supra*, and *Gulf Oil Corp.* v. *Lewellyn, supra* (the latter covered in principle by the first) cannot be regarded as laying down any general rule authorizing disregard of corporate entity in respect of taxation. These cases presented peculiar situations and were determined upon consideration of them. In the former this court said [p. 338]—'The case turns upon its very peculiar facts, and is distinguishable from others in which the question of the

identity of a controlling stockholder with his corporation has been raised. *Pullman Car Co.* v. *Missouri Pacific Ry. Co.*, 115 U. S. 587, 596; *Peterson* v. *Chicago, Rock Island & Pacific Ry. Co.*, 205 U. S. 364, 391'." (p. 420.)

See also *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435, 441-2.

Of course, the true limitation of any rule must be recognized. But that fact does not weaken the force of its effect within the sphere where it does operate, and the lower federal courts have applied the doctrine of *Southern Pacific Co.* v. *Lowe* whenever they have felt that the facts presented in a particular case warranted it. Thus, in *North Jersey Title Insurance Co.* v. *Commissioner*, 84 F. (2d) 898, the Circuit Court of Appeals for the Third Circuit discussed the doctrine and said "the present case presents just such 'peculiar circumstances' ". The facts in this case were that the insurance company had invested $400,000.00 in mortgages on properties of two real estate companies which had been represented to be improved properties but turned out to be vacant lots. The fraud was discovered and in order to protect its interest, the insurance company forced the real estate companies into receivership. It was decided that in order to protect the business of the insurance company, it would be necessary to avoid it becoming publicly known that titles had been insured on buildings that never existed, and so a subsidiary was organized to take over the properties of the real estate companies and deal with them for the insurance company. Eventually the insurance company acquired all the stock of the subsidiary and treated it as a real estate department of its own organization. The Circuit Court of Appeals held that losses sustained by the subsidiary might be deducted from the income of the parent insurance company. There was no question of the right to file consolidated returns in this case, the case being argued

solely on the theory that the corporate identity of the subsidiary might be disregarded. The following appears at page 901 of the opinion:

> "The principle that substance and not form should control in the application of income tax law is fundamental. Fictional corporate camouflage cannot be made the device to escape taxation. On the other hand, equal equity demands that the creation of a subsidiary corporate structure with no purpose of evading tax but solely for the purpose of meeting the exigencies of a serious and possible fatal financial situation should not be regarded as the birth of a new entity completely unidentified with the former for taxing purposes, particularly under the peculiar circumstances surrounding the instant case."

It is apparent from the record in the case at bar that the creation of Ohio was not "fictional corporate camouflage * * * to escape taxation," because there would never have been any problem as to the taxability of Glidden stock had the transaction been carried out without the creation of Ohio.

This same proposition is set forth by the Circuit Court of Appeals for the Second Circuit in *Munson S. S. Line* v. *Commissioner*, 77 F. (2d) 849. That case involved the application of the Merchant Marine Act of 1920 which permitted deductions from the war profits and excess profits taxes of the Act of 1918 in the amount of the net earnings of certain vessels documented under the laws of the United States and operated in foreign trade, The owner of the vessels was the person entitled to the deduction. The taxpayer involved claimed a deduction for eight vessels, the title to which was in subsidiary wholly-owned corporations. The vessels were registered in the names of the subsidiaries and were operated by the parent under charters from its subsidiaries "through stock ownership and identity of officers and directors, the petitioner exercised complete do-

minion and control of the vessels, collecting the revenues and paying the expenses * * *." The Circuit Court of Appeals for the Second Circuit said at page 851:

> "The situation is similar to that involved in *Southern Pacific Co.* v. *Lowe* * * * where the court held that there was practical identity between the Central Pacific and the Southern Pacific because of the complete ownership and control which the latter corporation possessed over the former. Thus even in tax cases the separate identity of corporations may be disregarded in exceptional circumstances. See, also, *Gulf Oil Corp.* v. *Lewellyn* * * *; *New Colonial Ice Co.* v. *Helvering* * * *. In our opinion to disregard it under the circumstances here disclosed will better carry out the legislative purpose of the statute in question."

It was also said earlier in the opinion:

> "The petitioner's argument that the broad construction for which it contends is more consonant with the purpose of promoting the investment in new American ships seems to us well taken. No reason is apparent, or has been suggested, why Congress should wish to limit its encouragement to corporate shipowners whose vessels were held directly and to exclude corporations which operated through wholly-owned subsidiaries."

Nor is any reason apparent to us why Congress should intend to interfere with corporate reorganizations involving valid business transactions where the requisite continuity of interest exists, merely because a wholly owned subsidiary corporation is injected into the picture solely to suit the convenience of the parent corporation, and for no other purpose.

There is another line of Circuit Court of Appeals cases which involve the problem of disregarding the separate corporate identity of wholly controlled subsidiaries. These are the cases holding that in certain instances a receiver appointed for the property of a parent may administer the subsidiary companies' properties also. Such a case is *Com-*

merce Trust Co. v. *Woodbury,* 77 F. (2d) 478, 487 (C. C. A. 8, 1935) ("There are cases which hold that a receiver of the parent company, under the order of the court, may take over the property of the subsidiaries.") Also in *Trustees System Co. of Pennsylvania* v. *Payne,* 65 F. (2d) 103 (C. C. A. 3, 1933), it is said (p. 107):

> "Through long practice courts have not hesitated to disregard the doctrine of corporate entities when the facts justify it. Although we know of no instance in which it has been done in matters of receivership, we cannot see why the same power does not exist in a court or why the law does not impose upon a court the same duty in a receivership matter when, as here, the facts are substantial enough to justify, indeed to compel, a finding that the five corporations were so identified with the parent corporation as to be a part of it. Being of opinion that the law makes no exception of receiverships, we tear asunder the legal maze of corporate fiction in which they have enveloped themselves and, observing that the six corporations were not merely related by stock ownership but, like wheels in a machine, were so closely meshed that all functioned together, we find from the bills that in legal effect they were one * * *."

In the case of *Centmont Corporation* v. *Marsch,* 68 F. (2d) 460 (C. C. A. 1, 1933), involving the point of whether a parent is entitled to share in the assets of a subsidiary in receivership, the court held that because of the control exercised by the parent over the subsidiary, the separate corporate entity must be disregarded.

To return to cases involving taxation, the case of *H. H. Miller Industries Co.* v. *Commissioner,* 61 F. (2d) 412 (C. C. A. 6, 1932), is helpful. That case involved the question of whether the deduction for exhaustion of a patent should be allowed a successor corporation as of the value on March 1, 1913, prior to which time the original corporation had acquired the patent, or upon the cost to the successor in 1918, at which time the successor company took over the assets

of the original corporation. The Board of Tax Appeals held that the basis for computing exhaustion was not March 1, 1913 value but the cost to the successor company at the date of organization and transfer of assets, upon the sole ground that the two corporations were technically separate and distinct taxable entities. The Circuit Court of Appeals reversed this decision, saying:

> "A taxing statute must be construed with regard to substance rather than to form. * * * Corporate entities are disregarded for tax purposes where subsidiary corporations are wholly owned by parent companies. *Southern Pacific Company* v. *Lowe*, * * *; *Gulf Oil Corporation* v. *Lewellyn* * * *. Where reorganization involves no change in capital structure, the new corporation is considered substantially a continuation of the old. *Weiss* v. *Stearn*, 265 U. S. 242 * * *."

and again at page 414:

> "We have here substantial identity of two corporations, with the same capital structure, same officers, and the same assets. Under these circumstances, to hold that they are two distinct taxable entities would be wholly to disregard substance and to emphasize mere form. Courts will not permit themselves to be blinded or deceived by mere forms of law, but, regardless of fictions, will deal with the substance of the transaction involved as if the corporate entity did not exist, and as the justice of the case may require."

Equally applicable is the statement which is made in *Osburn California Corp.* v. *Welch*, 39 F. (2d) 41 at 43:

> "The notion that a corporation is an entity separate and distinct from its stockholders is a fiction of law which the court will regard for some purposes and disregard for others. For tax purposes, this fiction is often disregarded."

An analysis of the facts in this case indicate that the peculiar circumstances are present which make this doctrine applicable. It is obvious that Ohio was organized by Glidden to carry on a new branch of its business that it was acquiring. Under the terms of the contract, Glidden

agreed to incorporate this subsidiary, Ohio, and had the sole power of determining its capitalization. Glidden was authorized by the contract to select the auditors who should determine the book value of the Indiana assets to be acquired. Glidden agreed to guarantee the payment of certain dividends on the Ohio stock to be issued to the Indiana stockholders. Glidden agreed to furnish all the cash to be paid by Ohio to Indiana stockholders.

It is stipulated that Glidden carried out all these agreements. In addition, it appears from the record (page 4) that Glidden paid the regular quarterly dividends upon the preferred stock of Ohio.

The foregoing shows that up to the time the stock in Indiana was acquired, Ohio was an empty shell with no assets except that it received from Glidden for 100 shares of its common stock a sum in cash which it, in turn, was to pay to the Indiana stockholders at Glidden's direction. Ohio was simply a receptacle formed by Glidden to receive the Indiana stock, and eventually the Indiana assets. Even after the stock of Indiana was transferred to Ohio, the stipulation of facts shows the extent of the control of Ohio by Glidden (R. 13):

> "Glidden and Company * * * caused the properties and assets of the Indiana Company to be conveyed and transferred to the new Ohio Company".

It is apparent that Ohio was simply an instrumentality used by Glidden to carry out this contract with the Indiana stockholders in order to acquire Indiana's assets for use in connection with its business. This control of a subsidiary so that it may be used as mere agency or instrumentality of a parent company is discussed in *Chicago, Milwaukee & St. Paul Ry. Co.* v. *Minneapolis Civic Association,* 247 U. S. 490, where at pages 500-501, it is pointed out that although mere ownership alone of capital stock of one

corporation by another does not create an identity of corporate interest, still

> "* * * where stock ownership has been resorted to not for the purpose of participating in the affairs of a corporation in the normal and usual manner, but for the purpose, as in this case, of controlling a subsidiary company so that it may be used as a mere agency or instrumentality of the owning company or companies."

the separate entities of the corporations would be disregarded. The court further said:

> "In such a case the courts will not permit themselves to be blinded or deceived by mere forms or law, but, regardless of fictions, will deal with the substance of the transaction involved as if corporate agency did not exist and as the justice of the case may require"

citing *United States* v. *Lehigh Valley Coal Co.*, 220 U. S. 247, 253, and *United States* v. *Delaware, Lackawanna and Western R. R. Co.*, 238 U. S. 516.

The parties to the transaction have thus themselves disregarded the separate corporate entity of one of the parties involved, not with any view to evading the tax burden, but entirely for their own convenience as a matter of business exigency. The courts should do likewise, since, as has often been said, taxation is a matter of substance and not form. *Weiss* v. *Stearn*, 265 U. S. 242 at 254.

Although not expressed in exactly these words, this court disregarded the corporate entity of the subsidiary corporation in the case of *Gregory* v. *Helvering*, 293 U. S. 465, where it was said (p. 469):

> "No doubt, a new and valid corporation was created. But that corporation was nothing more than a contrivance to the end last described. It was brought into existence for no other purpose; it performed, as it was intended from the beginning it should perform, no other function."

Even so, Ohio was created as a mere instrumentality for carrying out the purposes of Glidden, and as this court dis-

regarded the separate entity of the subsidiary in the *Gregory* case, so may the separate corporate entity of Ohio be disregarded in this case.

But the result of "piercing the corporate veil" in the two cases is entirely different. For in the *Gregory* case, if the formation of the subsidiary corporation is disregarded, the transaction clearly resulted in taxable gain, while if the formation of Ohio is disregarded in the instant case, there is admittedly no recognition of gain on receipt of the Glidden stock. And clearly the transfer in this case was made "in pursuance of a plan of reorganization" within the meaning of the Revenue Act.

Thus, in substance, Glidden acquired all the stock of Indiana and in essence performed the specific act constituting a reorganization of Indiana as described and defined in Section 112 (i) (1) (A). Applying even the narrowest test yet suggested, Glidden is then included under Section 112 (i) (2) by the language " 'a party to a reorganization' * * * includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation", since Glidden, through its instrumentality and *alter ego*, Ohio, acquired all the stock of Indiana.

Conclusion.

It is accordingly respectfully submitted:

1. That this case is one proper for the exercise by this court of its power of review by certiorari.

2. That the conflicts in decisions of the Circuit Courts of Appeals, the desirability of authoritative construction of the federal statute involved, and the inconsistency of the decision of the United States Circuit Court of Appeals for

the Seventh Circuit in this case with applicable decisions of this court, warrant the exercise by this court of its supervisory powers.

3. That the decision of the United States Circuit Court of Appeals for the Seventh Circuit is erroneous.

4. That for the reasons stated this court should review the decision of the United States Circuit Court of Appeals for the Seventh Circuit and upon hearing reverse it.

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APPENDIX.

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 112. RECOGNITION OF GAIN OF LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges solely in kind.*—

* * * * *

(3) STOCK FOR STOCK ON REORGANIZATION.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

* * * * *

(c) *Gain from exchanges not solely in kind.*—(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

* * * * *

(i) *Definition of reorganization.*—As used in this section and sections 113 and 115—

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if imme-

diately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

(j) *Definition of control.*—As used in this section the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.